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DOD PAYROLL WITHHOLDING DATA FOR FY 2000

Report No. D-2001-109

April 27, 2001

**Office of the Inspector General
Department of Defense**

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Abstract We performed this audit in response to the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, which requires DoD and other Government agencies to prepare consolidated financial statements. This audit supports our audit of the FY 2000 DoD Agency-Wide Financial Statements. Office of Management and Budget Bulletin No. 01-02, October 16, 2000, requires us to review the retirement, health, and life insurance withholdings and agency contributions during the course of conducting audits and specifies the procedures to apply. The DoD Financial Management Regulation prescribes the requirements of the Defense Finance and Accounting Service (DFAS) payroll accounting system. Specifically, the DFAS payroll accounting system is required to have the ability to query historical data, to provide audit trails, to provide management reports on an as-needed basis, and to support management reporting requirements. DoD has 12 agency payroll offices. The 12 payroll offices remitted more than \$2 billion to the Office of Personnel Management for FY 2000 in retirement, health, and life insurance withholdings and agency contributions for more than 690,000 DoD civilian employees with a total annual payroll of \$37.9 billion. The audit focused on 8 payroll offices that were responsible for paying more than 30,000 employees each. This report is the first of a series of reports on payroll withholding for FY 2000. We will report on the results of an expanded audit sample in a subsequent audit report.		

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Acronyms

CSRS	Civil Service Retirement System
DFAS	Defense Finance and Accounting Service
FERS	Federal Employees Retirement System
OPM	Office of Personnel Management
RITS	Retirement Insurance and Transfer System



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

April 27, 2001

**MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE**

**SUBJECT: Audit Report on DoD Payroll Withholding Data for FY 2000
(Report No. D-2001-109)**

We are providing this report for review and comment. We considered management comments on a draft of this report when preparing the final report. We conducted the audit in response to requirements of the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. As a result of management comments, we revised Recommendations 1. and 3. to cite other criteria and request a reconciliation of data differences. We request additional comments from Defense Finance and Accounting Service on Recommendations 1., 2., and 3. by June 27, 2001.

We appreciate the courtesies extended to the audit staff. For additional information on this report, please contact Mr. David F. Vincent at (703) 604-9110 (DSN 664-9110) (dvincent@dodig.osd.mil) or Mr. Thomas J. Winter at (703) 604-9134 (DSN 664-9134) (twinter@dodig.osd.mil). See Appendix B for the report distribution. We have listed the audit team members on the inside back cover of this report.

A handwritten signature in dark ink, appearing to read "Thomas F. Gimble", is positioned above the printed name.

Thomas F. Gimble
Acting
Deputy Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. D-2001-109

(Project No. D2000FH-0130.000)

April 27, 2001

DoD Payroll Withholding Data for FY 2000

Executive Summary

Introduction. We performed this audit in response to the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, which requires DoD and other Government agencies to prepare consolidated financial statements. This audit supports our audit of the FY 2000 DoD Agency-Wide Financial Statements. Office of Management and Budget Bulletin No. 01-02, October 16, 2000, requires us to review the retirement, health, and life insurance withholdings and agency contributions during the course of conducting audits and specifies the procedures to apply. The DoD Financial Management Regulation prescribes the requirements of the Defense Finance and Accounting Service (DFAS) payroll accounting system. Specifically, the DFAS payroll accounting system is required to have the ability to query historical data, to provide audit trails, to provide management reports on an as-needed basis, and to support management reporting requirements. DoD has 12 agency payroll offices. The 12 payroll offices remitted more than \$2 billion to the Office of Personnel Management for FY 2000 in retirement, health, and life insurance withholdings and agency contributions for more than 690,000 DoD civilian employees with a total annual payroll of \$37.9 billion. The audit focused on 8 payroll offices that were responsible for paying more than 30,000 employees each. This report is the first of a series of reports on payroll withholding for FY 2000. We will report on the results of an expanded audit sample in a subsequent audit report.

Objectives. Our objective was to determine whether the retirement, health, and life insurance withholdings and employee data submitted by DoD to the Office of Personnel Management for FY 2000 were accurate and supported. We also assessed management controls and compliance with laws, regulations, and procedures relative to payroll withholding data submitted by DoD.

Results. The DFAS and DoD personnel offices did not have adequate controls to support the accuracy of the payroll amounts withheld and remitted to the Office of Personnel Management.

For the three payroll periods tested, the \$247.5 million payroll withholding amount DFAS reported to the Office of Personnel Management exceeded the DFAS database by \$2.7 million. The overall difference was 1.09 percent. Although this is a small percentage difference, it represents a significantly higher error rate than the \$0.3 million, or 0.13 percent overall that we identified for FY 1999. As a result,

DFAS could not assure the accuracy of the DoD payroll withholding data transferred to the Office of Personnel Management. See Appendix A for details on the review of the management control program.

Summary of Recommendations. We recommend that the Director, DFAS, retain records as required by the DoD Financial Management Regulation to have an ability to query historical data, and to be able to generate as-needed reports to ensure the system's integrity. We recommend developing detailed accounting records, including software, to extract data to support the amounts reported to the Office of Personnel Management, and also retaining a separate exact electronic copy of the detailed data summarized into those reports. We recommend development of a system that maintains the support and justification for all payroll adjustments, including effects on payroll withholding reports, as well as providing reconciliation to the differences we noted in our FY 1999 and FY 2000 reports. We recommend that DFAS provide a reconciliation of the differences between what it reported to the Office of Personnel Management and the detail support provided to us.

Management Comments. The Director, Military and Civilian Pay Services, DFAS, nonconcurrent with all three recommendations and stated that the Defense Civilian Pay System currently maintains individual data items in support of the payroll withholding reports to the Office of Personnel Management for 26 pay periods. After 26 pay periods, DFAS maintains the data on microfiche at the St. Louis National Personnel Records Center. The Director, Military and Civilian Pay Services, DFAS, also stated that initial data provided by the DFAS was inaccurate because of miscommunication and misunderstanding of the requirements. The Director, Military and Civilian Pay Services, DFAS, also stated that the Defense Civilian Pay System currently provides audit trail information, which identifies the source of the adjustment and includes the dollar value and date of the adjustment. See the Finding and Management Comments sections in this report for details.

Audit Response. The comments from DFAS were not responsive. DFAS has not complied with the DoD Financial Management Regulation to maintain a capability to query historical data. It also has not been able to provide accurate and timely detail to support all payroll withholding reports to the Office of Personnel Management since 1999. Based on management comments, we revised the recommendation to develop or modify payroll systems to be in accordance with the DoD Financial Management Regulation. We revised the recommendation to develop an extraction query to add that DFAS also retain an exact electronic copy of the data summarized for reporting. We revised the recommendation to support and justify adjustments to payroll records to provide DFAS the opportunity to deliver an accurate database extraction that supports the summary amounts reported to the Office of Personnel Management for FY 1999 and FY 2000 because management responded that they have an audit trail to perform the task. We request that DFAS provide additional comments on the revised recommendations by June 27, 2001.

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Background

Reporting Requirements. Public Law 101-576, the “Chief Financial Officers Act of 1990,” November 15, 1990, requires Federal organizations to prepare annual audited financial statements. The Chief Financial Officers Act also requires the Inspectors General to audit all financial statements prepared under its guidelines. The Chief Financial Officers Act, as amended by Public Law 103-356, the “Federal Financial Management Act of 1994,” October 13, 1994, has required DoD and other Government agencies to prepare agency-wide financial statements since FY 1996.

Audits of Federal Financial Statements. Office of Management and Budget Bulletin No. 01-02, “Audits of Federal Financial Statements,” October 16, 2000, (the Bulletin) establishes responsibilities and standards for audits of Federal financial statements. Appendix I-1 of the Bulletin outlines agreed-upon procedures to be applied separately for each agency payroll office that services civilian employees during the year. The period subject to the agreed-upon procedures is for the 12 months ending September 30th of each year. On October 30, 2000, we submitted a separate memorandum report on the application of the agreed-upon procedures to the Inspector General of the Office of Personnel Management (OPM). This report identifies significant issues that were outside the reportable criteria of the agreed-upon procedures.

Payroll Responsibilities. The Defense Finance and Accounting Service (DFAS) provides payroll services to DoD, including calculation of gross pay, withholding, and reporting the amounts withheld to OPM. DFAS reports more than \$2 billion in withholding to OPM annually for more than 690,000 DoD civilian employees included in the total annual civilian payroll of approximately \$37.9 billion. DoD civilian personnel offices and regional centers are responsible for retaining the documentation that supports all DoD civilian personnel withholding elections and gross pay amounts.

Objectives

The overall audit objective was to determine whether the retirement, health benefits, and life insurance withholdings and employee data that DoD submitted to OPM for FY2000 were accurate and supported. Appendix I-1 of the Office of Management and Budget Bulletin No. 01-02 specifies the procedures that we applied to meet the objective. We also assessed management controls and compliance with laws, regulations, and procedures relative to payroll withholding data that DoD submitted. Appendix A includes a discussion of scope, methodology, the management control program review, and prior audit coverage.

Accuracy and Reliability of DoD Payroll Withholding Data

DFAS could not support the amount of DoD payroll withholding reported to OPM. Based on database tests for three payroll periods, the error rate for FY 2000 increased to 1.09 percent (\$2.7 million error out of \$247.5 million reported to OPM). The FY 2000 error rate of 1.09 percent compares to an error rate of 0.13 percent (\$0.3 million error out of \$230.9 million reported to OPM) in FY 1999. DFAS could not support the amounts reported to OPM because DFAS had a database that could be retroactively adjusted, and DFAS had not developed a query to accurately extract and archive the data reported. As a result, the payroll withholding amounts DoD reported to OPM are not accurate or reliable for financial reporting purposes.

Electronic Files

DFAS maintained and directly extracted data from a database known as the payroll history file. The database history retains data for 26 pay periods after the end of the pay period. However, the database is subject to retroactive processing and other changes. Because DFAS does not maintain exact payroll records to support amounts reported to OPM, it must task its computer staff to develop extraction routines to perform this function.

DoD Financial Management Regulation. DoD Regulation 7000.14-R, the DoD Financial Management Regulation, January 1998, and revisions (the Regulation) requires the DFAS payroll accounting system to have the ability to query historical data, to provide audit trails, to provide management reports on an as needed basis, and to support management reporting requirements. The Regulation, volume 8, chapter 1, August 1999, paragraph 010201.B.8. and 9., requires the payroll accounting system to be able to query current and historical data, and to provide an audit trail that permits the tracing of transactions through the system. The Regulation, volume 8, chapter 9, August 1999, paragraph 090201 requires the payroll accounting system to be able to generate reports on an as-needed basis or by producing reports to meet special requirements to test the integrity of the system. The Regulation, volume 13, chapter 8, paragraph 080102.D.1. and 3., January 1998, requires the payroll accounting system to support management purposes including internal and external reporting requirements.

Audit Trails and Adjustments. The Regulation, volume 6A, chapter 2, "Departmental Financial Reports Roles and Responsibilities," February 1996, assigns departmental financial reporting roles and responsibilities. The Regulation, volume 6, chapter 2, January 1998, (paragraph 020203, "Audit Trails") requires DFAS to verify that a complete and documented audit trail is maintained to support the reports it prepares. Further, the audit trail should include verification that the numbers, types, and dollar amounts of transactions received from customers, as well as those generated by DFAS, are processed

timely and entered accurately into the finance and accounting systems. In addition, all transactions, with an effective date of the current reporting period, are included in the data for that reporting period. The Regulation, volume 6, chapter 2, also states that DFAS must support adequately and justify in writing any adjustment to the official accounting records, and provide an audit trail to the source transactions that required the adjustment. For adjustments, the documentation must include the rationale and justification for the adjustment, dollar amounts proposed for adjustment, and the date of the adjustment. The Regulation, volume 8, chapter 1, "Civilian Pay Policy and Procedures," August 1999, prescribes objectives and related requirements for DoD civilian employee pay operations and systems. DoD payroll operations and systems must also interface with the general ledger and personnel functions, with provisions for reconciling common data elements in separate systems to one another. Audit trails also are required to permit the tracing of transactions through the payroll system.

Database Transfer and Footing. For this audit, DFAS extracted payroll data files from the Defense Civilian Pay System payroll databases and sent it by an electronic file transfer procedure. We added the 24 payroll data files (8 payroll offices with more than 30,000 employees each for 3 pay periods) with more than \$3.33 billion in total pay (approximately \$1.1 billion per 2-week pay period) and more than 600,000 employees in each payroll period. We also added withholding amounts for life insurance, health insurance, Civil Service Retirement System (CSRS), and Federal Employees Retirement System (FERS).

Comparison of Database to Footings. We traced the employee withholding totals to the related amounts shown on the Retirement Insurance and Transfer System (RITS) submission. As listed in the table below, the payroll data file totals did not equal the amounts reported to OPM. DFAS was unable to provide us the exact detailed information that supports the amounts it previously reported to OPM because the DFAS developed a query that could not provide all the detail necessary to match the amounts. The amounts withheld for life insurance, health insurance, CSRS, and FERS were usually less than the withholding amounts reported to OPM in the RITS submission data. The total difference and percentage difference are shown in the table.

RITS Data Submissions Exceeded Payroll Data Files				
<u>Type of Withholding</u>	<u>Reported to OPM (millions)</u>	<u>Total of DFAS Data (millions)</u>	<u>Total of Differences (millions)</u>	<u>Percent Difference</u>
Life Insurance	\$ 30.20	\$ 29.86	\$ 0.34	1.13
Health Insurance	83.00	82.20	0.80	0.96
CSRS	114.30	112.93	1.37	1.19
FERS	20.00	19.79	0.21	1.05
Total	\$ 247.50	\$ 244.78	\$ 2.72	1.09

The total withholding that DFAS reported to OPM for the three payrolls tested in FY 2000 was \$247.5 million. The amounts reported to OPM exceeded the totals of the database that DFAS provided by \$2.7 million, or 1.09 percent. This was a significant increase in the error rate from the FY 1999 payroll data. The total withholding reported to OPM for the three payrolls tested in FY 1999 was \$230.9 million. The amounts reported to OPM in FY 1999 were less than the databases by \$0.3 million, or 0.13 percent. We originally reported the need for extraction software in Inspector General, DoD, Report No. D-2000-156, "DoD Payroll Withholding Data for FY 1999," June 29, 2000. However, because of the increased error rate between FY 2000 and FY 1999 and the need to accurately report payroll data to OPM, we consider the differences in the amounts to be a material management control weakness.

Retroactive Adjustments and Extracting Data. The differences occurred because DFAS maintained a database that could be retroactively adjusted, and DFAS did not accurately extract data that was in its database. Specific examples of adjustments would be for pay increases and changes in employee deductions for health or life insurance. Using its current extraction routines, DFAS was unable to provide details concerning differences between the official personnel file and amounts reported by DFAS. DFAS needs to develop the information system capability to support and justify adjustments to payroll records, including dollar amounts, and dates of the adjustments. DFAS also needs to provide an audit trail to the source transactions that generated the adjustment. Even small discrepancies reduce the reliability, accuracy, and verifiability of personal payroll data of individuals transmitted to OPM.

DFAS can improve the capability to provide exact data support for the amounts reported to OPM by excluding retroactive adjustments and other changes. Also, DFAS explained that it did not include the payroll files of inactive employees and employees with no gross pay in response to our data request. DFAS was

unable to provide us with the details for inactive employees or employees with no gross pay because its developed program was inadequate to extract the amounts from its database. We discussed alternative electronic methods, and DFAS personnel are investigating the possibility of developing an improved program for required audits in the future. After DFAS develops the program, it should total the data it extracted and compare the totals with the amounts it previously reported to OPM to test the accuracy.

Conclusion

DFAS maintains a payroll history database for 26 pay periods that is subject to retroactive adjustment. This results in a situation in which the payroll withholdings and the amounts reported to OPM cannot be reconciled. DFAS needs an ability to query historical data to test payroll and withholding amounts for each payroll period. In addition, DFAS needs to record all adjustments made to payroll records, including dollar amounts and dates of the adjustments, and, DFAS needs to provide an audit trail to the source transactions that required adjustment. Further, DFAS needs to develop a data query capable of extracting details in electronic payroll data previously summarized and transmitted to OPM for withholding payments.

Recommendations, Management Comments, and Audit Response

Revised Recommendations. As a result of management comments, we revised Recommendation 1. to specifically cite the DoD Regulation 7000.14-R, the DoD Financial Management Regulation, May 1993 with changes through April 2001, and we added a section that requires management to have the ability to query historical data to test the payroll system integrity. We revised Recommendation 2. to include an electronic copy of the summarized data reported. We also revised Recommendation 3. to include a statement that the Defense Finance and Accounting Service provide a reconciliation for the differences noted in this report and a prior IG, DoD, report.

We recommend that the Director, Defense Finance and Accounting Service:

1. Develop or modify payroll systems to maintain the data summarized for reports to Office of Personnel Management consistent with DoD Regulation 7000.14-R, the DoD Financial Management Regulation, May 1993 with changes through April 2001, that would allow for the capability to query historical data.

Management Comments. The Director, Military and Civilian Pay Services, Defense Finance and Accounting Service, nonconcurred with the draft report recommendation, stating that the Defense Civilian Pay System currently maintains individual data items in support of the summarized reports to the

Office of Personnel Management as required by the National Archives and Record Administration, General Schedule 2. Employer contribution and employee deduction data are maintained on-line at the employee level for 26 pay periods. The data are available for on-line viewing and are retrievable for audit purposes through an ad hoc query process. After 26 pay periods, the Master Pay, Leave and Time history data are stored on microfiche which are sent quarterly to the National Personnel Records Center, Civilian Records Center, St. Louis, MO.

Audit Response. The Defense Finance and Accounting Service comments were not responsive. Because the Defense Finance and Accounting Service allows the database to lapse after 26 pay periods, it is not following the requirements of the DoD Regulation 7000.14-R, the DoD Financial Management Regulation, volume 8, chapter 1, revised August 1999, for civilian payroll retention. The Regulation requires the payroll system to have the capability to query current and historical data, and have an audit trail that permits tracing of transactions. The Regulation, volume 8, chapter 9, August 1999, also requires the payroll system to be able to generate as-needed reports for management to ensure the system's integrity, such as summaries provided to the Office of Personnel Management. The loss of the database after 26 pay periods significantly limits the opportunity for the Defense Finance and Accounting Service management to query civilian employee payroll data at a macro and micro level, which is necessary in order to perform the Office of Personnel Management audit, and accomplish other management inquiries affecting the system. Retrieval of microfiche archived data at the records center on a regular basis would be impractical, costly, and not permit Defense Finance and Accounting Service management the ability to manage the database. We request that the Director, Defense Finance and Accounting Service, comment on this revised final report recommendation.

2. Develop an extraction query capable of extracting exact details in electronic payroll data summarized and transmitted to Office of Personnel Management for withholding payments, and also retain a separate exact electronic copy of the data summarized into those summary reports.

Management Comments. The Director, Military and Civilian Pay Services, Defense Finance and Accounting Service nonconcurrent and stated that the initial data it provided were incomplete or inaccurate in some instances because of miscommunication or misunderstanding of the requirements. A subsequent file provided to support the reporting to the Office of Personnel Management contained complete data and omitted nonpertinent data. If the subsequent file had been used to complete the audit, the differences between the amounts reported to Office of Personnel Management and the amounts supported from the database would have been significantly smaller.

Audit Response. The Defense Finance and Accounting Service provides summary payroll withholding reports to the Office of Personnel Management for the elements of retirement, health insurance, and life insurance, based on its detail supporting records. The data used to support the summary report sent to the Office of Personnel Management continued to change. The changes in the database need to be eliminated when a query is activated later. We performed

the Office of Management and Budget agreed-upon procedures for payroll withholding and requested that the Defense Finance and Accounting Service provide an electronic copy of the database that it used to prepare the summary withholding reports to the Office of Personnel Management. Because the Defense Finance and Accounting Service has a database that is constantly changing, they had difficulty extracting the detail used to support the previously reported summaries to the Office of Personnel Management. The Defense Finance and Accounting Service has been unable to provide us with the detailed information that we could audit to arrive at the same totals it reported in summary to the Office of Personnel Management. We have requested this same detailed information for two concurrent years and the Defense Finance and Accounting Service has been unable to provide it.

The Defense Finance and Accounting Service's explanation that misunderstandings and miscommunication of the requirements caused the data to be inaccurate is not consistent with the results of the review. The Defense Finance and Accounting Service retains information supporting payroll that is constantly changing. To extract the data requires programmers to develop a query that ignores changes, which can take weeks or months to provide results. The Defense Finance and Accounting Service's explanation that misunderstandings or miscommunication caused the payroll data to be inaccurate obscures the difficulty of accurately supporting the detail of a payroll withholding report prepared from a previous version of a database. The database used ignores the requirement in the DoD Financial Management Regulation to maintain an audit trail to permit the tracing of transactions through the payroll system, because summary amounts cannot be readily traced to the individual transaction.

The Defense Finance and Accounting Service provided management comments on April 12, 2000, that we included in Inspector General, DoD, Report No. D-2000-156, "DoD Payroll Withholding Data for FY 1999," June 29, 2000. The Defense Finance and Accounting Service commented that the data extraction query requirements would be refined and in place for future audits. However, the Defense Finance and Accounting Service did not develop an accurate and timely data extraction query, so the subsequent data files were not available in time to meet our payroll audit required by Office of Management and Budget Bulletin 01-02 for FY 2000. Even though data supporting payroll withholding reports were originally requested in 1999 for an annual audit requirement, the Defense Finance and Accounting Service provided amounts in its recent data file in support of Federal employee health benefits that disagreed with payroll withholding reports by \$36,754. The Defense Finance and Accounting Service has significantly improved its accuracy to arrive at a potential reconciliation, but it has occurred during our three requests and required approximately 19 weeks for them to respond. These 19 weeks have required programmers time to extract what we anticipated would be readily available and accurate. Even after our three requests for data, the Defense Finance and Accounting Service has still not developed a capability to provide exact support for the amounts it reports to the Office of Personnel Management. We request that the Director, Defense Finance and Accounting Service, comment on this revised final report recommendation.

3. Develop and provide the information system capability to support and justify adjustments to payroll records, including dollar amounts and dates of the adjustments, and provide an audit trail to the source transactions that required the adjustment. Provide a reconciliation to the differences we noted in Inspector General, DoD, Report No. D-2000-156, "DoD Payroll Withholding Data for FY 1999," June 29, 2000 and this report to confirm an audit trail exists.

Management Comments. Defense Finance and Accounting Service nonconcurred with the draft report recommendation and stated that the Defense Civilian Pay System currently provides audit trail information, which identifies the source of the adjustment and includes the dollar value and date of the adjustment. Some of this information is in the Master Employee History records that are retained for approximately one year as described in management comments concerning Recommendation 1. Additional information concerning adjustment records is captured on reports provided to the payroll office for review and retention. The Master Employee Add/Change/Delete Report and the Adjustment of Hours and Amounts Report can be used to determine the source of an adjustment.

Audit Response. The Defense Finance and Accounting Service could not provide us with accurate detail to support the payroll withholding reports it sent to the Office of Personnel Management. Although the Defense Finance and Accounting Service has identified audit trail information for adjustments to payroll records for individual civilian employees, it has not identified audit trail information for adjustments to payroll records that would affect payroll withholding reports. When the Defense Finance and Accounting Service provided database files that did not total to the payroll withholding amounts reported to the Office of Personnel Management during the audit of DoD Payroll Withholding Data for FY 1999, they explained that the differences were due in part to retroactive changes to its payroll records. At that time, we discussed alternative systems with the Defense Finance and Accounting Service payroll personnel and agreed to recommend an improved capability to provide exact data supporting payroll withholding. In order to provide exact data supporting payroll withholding, the Defense Finance and Accounting Service needed to develop the capability to provide support for the amounts reported to the Office of Personnel Management in payroll withholding reports, excluding retroactive adjustments and other changes. For FY 2000, we have subsequently requested data supporting amounts reported to the Office of Personnel Management in payroll withholding reports, and the Defense Finance and Accounting Service has not been able to provide exact detailed support for all of the amounts reported. The Defense Finance and Accounting Service needs to determine how adjustments to its payroll database affect the amounts reported to the Office of Personnel Management in payroll withholding reports and to have a capability to identify and summarize those adjustments for each payroll withholding report.

According to the agreed-upon procedures in Office of Management and Budget Bulletin 01-02, "Audits of Federal Financial Statements," October 16, 2000, all of the differences between the payroll register databases and the amounts reported to the Office of Personnel Management are to be reconciled and

explained. The Defense Finance and Accounting Service should provide a reconciliation to the differences we noted in our FY 1999 and FY 2000 reports in order to support their contention that they have an adequate audit trail that provides those details with the existing systems they have in place. We request that the Director, Defense Finance and Accounting Service, provide comments on this revised final report recommendation.

Appendix A. Audit Process

Scope

We reviewed the data and documentation supporting the \$2 billion in payroll withholding reported during each year by DFAS to OPM for DoD civilian personnel. The total annual payroll for 690,000 DoD civilian employees is \$37.9 billion. We selected for review the payroll files and supporting documentation for the payroll periods that ended January 29, 2000; February 26, 2000; and April 22, 2000, from the computer-processed data in the DFAS payroll history database. The DFAS payroll history database did not support the amount of DoD payroll withholding reported to OPM, and we made recommendations addressing this deficiency for FY 1999 in Inspector General, DoD, Report No. D2000-156 issued June 29, 2000. We found the DFAS payroll history database was usable for audit purposes for individual audit sample items we selected. We also reviewed DoD plans and actions to automate and use electronic media to record DoD civilian personnel withholding elections.

DoD-Wide Corporate Level Government Performance and Results Act Coverage. In response to the Government Performance Results Act, the Secretary of Defense annually establishes DoD-wide corporate level goals, subordinate performance goals, and performance measures. This report pertains to achievement of the following goal, subordinate performance goal, and performance measures.

FY 2001 DoD Corporate Level Goal 2: Prepare now for an uncertain future by pursuing a focused modernization effort that maintains U.S. qualitative superiority in key warfighting capabilities. Transform the force by exploiting the Revolution in Military Affairs, and reengineer the Department to achieve a 21st century infrastructure. **(01-DoD-2)** **FY 2001 Subordinate Performance Goal 2.5:** Improve DoD financial and information management. **(01-DoD-2.5)** **FY 2001 Performance Measure 2.5.2** Achieve unqualified opinions on financial statements. **(01-DoD-2.5.2)**

DoD Functional Area Reform Goals. Most major DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following functional area objective and goal.

- **Financial Management Objective:** Strengthen internal controls.
Goal: Improve compliance with the Federal Managers' Financial Integrity Act. **(FM-5.3)**

General Accounting Office High-Risk Area. The General Accounting Office has identified several high-risk areas in the DoD. This report provides coverage of the Defense Financial Management high-risk area.

Audit Type, Dates, and Standards. We performed this financial-related audit from April through December 2000 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Accordingly, we included tests of management controls considered necessary.

Contacts During the Audit. We visited or contacted individuals and organizations within DoD and the Office of Personnel Management. Further details are available upon request.

Methodology

We reviewed data and documentation supporting gross pay and payroll withholdings reported by DFAS to OPM. We also reviewed internal controls over the reporting process, including whether DFAS could provide subsidiary payroll withholding records that totaled the amounts reported for payroll withholding to OPM. We electronically obtained the payroll data files from the payroll history database at Pensacola by a file transfer procedure from DFAS. We independently totaled the 24 payroll data files (the 8 payroll offices with more than 30,000 employees each for 3 pay periods). The data files represent about 600,000 employees for each pay period. We compared the totals of each payroll data file with the amounts reported to OPM through the RITS on Form 2812. For the three pay periods selected, we compared the total of the total column on the Forms 2812 with the actual amount transferred.

Computer-Processed Data. We did not evaluate the general and application controls of the Defense Civilian Pay System that processes payroll data, although we did rely on data produced by that system to conduct the audit. We did not evaluate the controls because we determined data reliability by adding the data provided to us from the system and comparing the totals to summary documents previously prepared from data in the system. Not evaluating the controls did not affect the results of the audit.

Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996 and DoD Instruction 5010.40, "Management Control Program Procedures," August 28, 1996, require DoD managers to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of those controls.

Scope of Review of Management Control Program. We reviewed the annual statement of assurance by DFAS for FY 1999. We reviewed the report to determine whether it disclosed the lack of software capable of extracting exact details in the electronic payroll data summarized and transmitted to OPM for withholding payments.

Adequacy of Management Controls. We identified a material management control weakness, as defined by DoD Instruction 5010.40. DFAS did not have the software capability to extract exact details in the electronic payroll data summarized and transmitted to OPM for withholding payments. Recommendations 1. and 2., in this report, if implemented, will improve the accuracy of database support for the amounts that DFAS summarizes to report to OPM.

Adequacy of Management's Self-Evaluation. Management's self-evaluation did not identify the material weakness because management did not identify the area as an assessable unit. In addition, the DFAS management letter of assurance did not identify the material management control weakness because a prior review of DoD payroll withholding data, performed by a contractor, omitted some of the agreed-upon procedures, and therefore, did not disclose the weakness.

Management Comments on Control Program Review. Defense Finance and Accounting Services disagreed that it had a material management control weakness. The Defense Finance and Accounting Service stated that after a review of the audit requirements, a second data file was created that contained accurate, supportable data. However, the Defense Finance and Accounting Service added that it is exploring an alternative method of data storage or retrieval. This requirement is being driven by a soon to be implemented system change which will allow the mechanized transfer of employee data, including history data, between databases. This mingling of history data will negatively affect the ability to provide accurate detail data to support the summary data reported to OPM. A System Change Request is being written to develop an alternative methodology to accomplish this requirement.

Audit Response. An audit trail from summary payroll withholding reports submitted to OPM to the detail in the DFAS database from which those reports were summarized is essential to safeguard the accuracy. The Regulation, volume 8, chapter 1, August 1999, states that DoD payroll operations and systems shall have audit trails to permit the tracing of transactions through the payroll system. The inability of Defense Finance and Accounting Service to provide an audit trail from summary withholding reports to OPM to the detail in the database is a significant deficiency, and therefore, a material management control weakness.

Prior Coverage

The Inspector General, DoD, and the Air Force Audit Agency have conducted multiple reviews related to civilian payroll information, controls over the payroll process, and payroll expenses. Unrestricted Inspector General, DoD, reports can be accessed on the Internet at www.dodig.osd.mil. Unrestricted Air Force Audit Agency reports can be accessed on the Internet at www.afaa.hq.af.mil.

Appendix B. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Auditor General, Department of the Air Force

Other Defense Organizations

Director, Defense Finance and Accounting Service
Director, Civilian Personnel Management Service

Non-Defense Federal Organizations

Office of Management and Budget
Office of Personnel Management

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Efficiency, Financial Management, and Intergovernmental Relations, Committee on Government Reform
House Subcommittee on National Security, Veterans Affairs, and International Relations, Committee on Government Reform
House Subcommittee on Technology and Procurement Policy, Committee on Government Reform

Defense Finance and Accounting Service Comments

Final Report
Reference



DEFENSE FINANCE AND ACCOUNTING SERVICE
KANSAS CITY, MISSOURI 64197-0001

FEB 13 2001

DFAS-PSC/PE

MEMORANDUM FOR INSPECTOR GENERAL, DEPARTMENT OF DEFENSE,
ARLINGTON, VIRGINIA

SUBJECT: DFAS Comments on Draft Audit Report on DoD Payroll
Withholding Data for FY 2000 (Project No. D2000FH-
0130.000) dated December 13, 2000

The Defense Finance and Accounting Service, Military and
Civilian Pay Services comments to the subject draft audit report
are attached. We appreciate the opportunity to review and
provide comments on this report.

Questions your staff may have concerning these matters may
be directed to my point of contact, Ms. Sandy Barrineau,
DFAS-PSC/PE, (850) 452-2990 extension 562 or DSN 922-2990
extension 562.

A handwritten signature in black ink, appearing to read "S. E. Turner", is positioned above the printed name of the Director.

Steve E. Turner
Director, Military and Civilian Pay Services

Attachment:
As stated

cc: DFAS-AR/DDI

(not included)

Final Report
Reference

Revised

DFAS Comments on Draft Audit of the DoD Payroll Withholding
Data for FY 2000 (Project No. D2000FH-0130.000)

Recommendations:

Recommendation 1: "We recommend that the Director, Defense Finance and Accounting Service develop or modify systems to maintain the data summarized for reports to OPM as required by the National Archives and Record Administration, General Schedule 2."

DFAS Comments: Non-concur.

Rationale for Non-concurrence: The Defense Civilian Pay System (DCPS) currently maintains individual data items in support of the summarized reports to OPM as required by the National Archives and Records Administration, General Schedule 2. Employer contribution and employee deduction data are maintained on-line at the employee level for 26 pay periods. The data is available for on-line viewing and is retrievable for audit purposes through an ad hoc query process. After 26 pay periods the Master Pay, Leave and Time history data are stored on microfiche which are sent quarterly to the National Personnel Records Center, Civilian Records Center, St. Louis, MO.

Revised

Recommendation 2: "Develop an extraction query capable of extracting exact details in electronic payroll data summarized and transmitted to OPM for withholding payments."

DFAS Comments: Non-concur.

Rationale for Non-concurrence: The initial data provided by DFAS was incomplete or inaccurate in some instances due to miscommunication or misunderstanding of the requirements. Inclusion of history or memo records, year to date adjustment records, and inaccurate handling of the family multiplier for life insurance were some of the causes of inaccurate data in the first query. A subsequent query file to support the reporting to OPM was provided. This file contained complete data and omitted non-pertinent data. If this file had been used to complete the audit, the findings would have been well within allowable deviations. A spreadsheet supporting this position and based on the data requirements as stated in the Inspector General's memorandum of August 24, 2000 for Joseph Campbell, Director for Civilian Pay, is attached for your review.

(not included)

Revised

Pages 10-11

Recommendation 3: "Develop the information system capability to support and justify adjustments to payroll records, including dollar amounts, date of the adjustment, and provide an audit trail to the source transactions that required adjustment."

DFAS Comments: Non-concur.

Rationale for Non-concurrence: DCPS currently provides audit trail information, which identifies the source of the adjustment and includes the dollar value and date of the adjustment. Some of this information is retained in the Master Employee History records that are retained as described in our comments concerning Recommendation 1. Additional information concerning adjustment records is captured on reports provided to the payroll office for review and retention. The Master Employee Add/Change/Delete Report and the Adjustment of Hours and Amounts Report can be used to determine the source of an adjustment.

Management Control Weakness:

Adequacy of Management Controls (Page 7): "We identified a material management control weakness, as defined by DoD Instruction 5010.40, Management Control Program Procedures, dated August 28, 1996. DFAS did not have the software capability to extract exact details in the electronic payroll data summarized and transmitted to OPM for withholding payments."

DFAS Comments: The methodology used to retrieve the data for this audit was an ad hoc query. The parameters for these queries are established based on the understanding of the data requirement. As stated in our response to the recommendations, the initial data provided was flawed and incomplete. After a review of the requirements, a second file was created and contained accurate, supportable data.

While we do not feel this situation constitutes a material weakness, an alternative method of data storage or retrieval is being explored. The requirement is being driven by a soon to be implemented system change which will allow the mechanized transfer of employee data, including history data, between databases. This mingling of history data will negatively impact the ability to provide accurate detail data to support the summary data reported to OPM. A System Change Request is being written to develop an alternative methodology to accomplish this requirement.

Audit Team Members

The Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report. Personnel of the Office of the Inspector General, DoD, who contributed to the report are listed below.

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